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UNCLAS SECTION 01 OF 02 ANKARA 000503

SIPDIS

SENSITIVE

TREASURY FOR OASIA -- RADKINS, CPLANTIER
NSC FOR BRYZA AND MCKIBBEN

E.O.12958: N/A
TAGS: EFIN TU
SUBJECT: Turkish Central Bank Intervenes: Motives Unclear

REF: ANKARA 197

SENSITIVE BUT UNCLASSIFIED.

¶1. (SBU) Summary: The Turkish Central Bank made a rare direct intervention in foreign exchange markets on January 27, buying about $1.5 billion to control excess foreign exchange (FX) market volatility and excess FX liquidity. This is the first direct intervention since February 2004 when the Bank bought USD 1.3 billion. There had been market worries about the level of the New Turkish Lira rate, which had appreciated rapidly against foreign currencies since December 17. Yet, the Central Bank denies that intervention was engineered to depreciate the lira. End Summary.

¶2. (SBU) In a January 27 press statement, the Central Bank said that the level of exchange rate was determined by supply and demand conditions of the currency markets under the floating exchange rate regime. The Central Bank, however, closely monitored the volatility of the rates and reserved the right to directly intervene in the market in conditions of excess volatility. According to the statement, recent excessive volatility in exchange rates was due to an increased supply of foreign exchange. The Central Bank decided to intervene directly in the markets by buying foreign currency and noted that the fact of the intervention should not be connected with the level of the lira.

¶3. (SBU) However, in their comments on the intervention, Turkish market players speculated that the lira's current level was indeed the main motivation and that the Bank's action should not have come as a surprise. Market traders said they had been expecting an intervention if the TRL/USD rate went below 1.34. The Central Bank started to intervene at 1.3215 January 27, leaving the rate at 1.3490 at the end of the day. As expected, the level of the exchange rate again provided a selling opportunity January 28, with the TRL/USD rate closing the day at 1.3351 and TRL the continuing its appreciation despite yesterday's strong intervention.

¶4. (SBU) Market sources estimated the total amount of the intervention at $1.2 billion. Central Bank Market Department DG Cigdem Kose told Econ Specialist that the total amount of intervention was somewhere between $1.2 and 1.5 billion. This compares with a total amount bought by the CBRT of $677.3 million since market FX auctions resumed on December 22, of which $241.6 million was bought in December. Daily auction amounts had been in a range of $15-20 million.

¶5. (SBU) Kose said that the Bank had been observing significant market volatility since December 10. The lira's appreciation against the dollar had been approximately 8 percent since December 10, and 6 percent since January 6. This, Kose said, was due to a significant increase in FX flow. Between December 17 and January 14, the CBRT was able to capture about $2 billion in foreign inflows. Additionally, a significant foreign demand came from Treasury's domestic borrowing auction this week in which it sold a net total of 3.5 billion new TRL to the markets (USD 2.7 billion). Furthermore, new TRL denominated issuance by foreign issuers since the beginning of the year amounted to about new TL 1 billion ($750 million). All these of flows caused a significant pressure on the TRL's level in the FX market, Kose said. Kose also noted that on January 27 the CBRT observed a significant flow into Turkey from the NY markets. Cigdem Kose noted that the CBRT would not consider changing its daily FX buying amount in the future, but could consider intervening again as required.

¶6. (SBU) Comment: In short, Kose said that excess FX

liquidity and high volatility were the two main causes for the Central Bank intervention decision on January 27, but it seems that the Bank's rare activism (apart from the daily auction process) was unable to control the volatility that resumed January 28. The Bank's action does not appear to reflect a change in basic policy, which has always reserved the right to intervene to control unstable market conditions. State Minister Babacan said yesterday that the Turkish government did not favor direct intervention under the free float regime, and that it preferred to keep any necessary interventions to a minimum. This remark seems at some variance to the CBRT's thinking. End Comment. DEUTSCH